



# Financial Management Report

AS OF JUNE 30, 2007

## AT A GLANCE:

General Fund revenues ahead of last year by 5.1 percent.

Sales tax up 9.4 percent (see page 5)

Development revenue down overall (see page 3)

Puget Sound region is expected to add 100,000 jobs over the next two years, contributing to an economy that will out-perform the rest of the nation.

Local housing sales fall, but prices rise (see pages 7-8).

Global economic conditions expected to create positive growth in local area.

Washington State exports up 10.6% for first quarter 2007 compared to the first quarter of 2006.

Costco in Bellevue? (see page 7)

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## Summary of All Operating Funds: *Revenue*

- **General Fund** revenue is budgeted to increase 6.8 percent in 2007 over 2006, largely from expectations of higher sales and utility tax revenue and property tax dedicated to public safety staffing. Actual revenues are trailing the budgeted increase at 5.1 percent ahead of the same period last year, largely due to a dip in building permit revenues and despite strong sales and utility tax revenue and plan check development fees. Total General Fund revenues are expected to track at or above budget as the year progresses.
- **Other General Government Funds** revenues are budgeted 10 percent higher in 2007 than last year largely due to increased internal charges and the move of Multi-media Services from the General Fund to the Information Technology Fund. Actual collections are tracking higher than planned, at 14.3 percent ahead of the same period last year, mostly due to the receipt of 2006 cable tax revenue in 2007.
- **Water Sewer Operating Fund** revenue is budgeted 4.3 percent higher in 2007 than 2006 due to water and sewer rate increases and normal growth. Actual revenue is tracking higher than expected, at 11.3 percent due to strong water sales this year.
- **Surface Water Management Fund** revenue collection is budgeted 4.9 percent higher in 2007 than 2006 due to rate increases and normal growth. Actual revenue is trailing the planned increase at 0.7 percent ahead of the same period last year. Surface Water fees are paid through property tax collection, which are primarily received in April and October. However, property tax is also paid when real estate is sold. The active real estate market last year may have resulted in more revenue being received outside the normal timing of April and October. This year may be returning to more normal trends.
- **Solid Waste Fund** revenue collection is budgeted to increase 5.6 percent in 2007 over 2006 due to higher rates and normal growth. Actual revenue is tracking slightly lower than planned, at 3.6 percent ahead of the same period last year due to variability in collections for this utility. Revenue is expected to track at budget as the year progresses.

Resources by Fund	Year-to-Date Actual			Budget			% of Budget	
	6/30/2006	6/30/2007	% Change	2006	2007	% Change	2006	2007
<b>General Gov't Operating:</b>								
General Fund	23,974,376	25,189,201	5.1%	49,091,816	52,445,710	6.8%	48.8%	48.0%
Other General Gov't Operating Funds	7,443,127	8,504,422	14.3%	15,170,554	16,683,646	10.0%	49.1%	51.0%
<b>Total General Gov't Operating</b>	<b>31,417,503</b>	<b>33,693,623</b>	<b>7.2%</b>	<b>64,262,370</b>	<b>69,129,356</b>	<b>7.6%</b>	<b>48.9%</b>	<b>48.7%</b>
<b>Utilities:</b>								
Water/Sewer Operating Fund	6,696,379	7,451,896	11.3%	15,802,180	16,474,571	4.3%	42.4%	45.2%
Surface Water Management Fund	2,730,836	2,749,852	0.7%	4,977,108	5,222,394	4.9%	54.9%	52.7%
Solid Waste Fund	3,741,884	3,876,838	3.6%	7,449,930	7,864,908	5.6%	50.2%	49.3%
<b>Total Utilities</b>	<b>13,169,099</b>	<b>14,078,586</b>	<b>6.9%</b>	<b>28,229,218</b>	<b>29,561,873</b>	<b>4.7%</b>	<b>46.7%</b>	<b>47.6%</b>
<b>Total All Operating Funds</b>	<b>44,586,602</b>	<b>47,772,209</b>	<b>7.1%</b>	<b>92,491,588</b>	<b>98,691,229</b>	<b>6.7%</b>	<b>48.2%</b>	<b>48.4%</b>

\* Budgeted and actual revenues exclude resources forward and include interfund transfers.



Surface Water Utility rates were increased in 2006 as a result of the Master Plan adopted in 2005 that identified operating and capital projects. The additional resources provide a much greater ability for the City to protect and enhance its natural environment as illustrated by the streambank stabilization project pictured above.

## Summary of All Operating Funds: *Expenditures*

- **General Fund** expenditures are budgeted to increase 8.3 percent in 2007 over 2006 largely due to increased personnel costs and additional staffing, as well as budgets for unfinished projects "carried over" from the prior year. Actual expenditures are 11.8 percent ahead of the same period last year primarily due to the settlement of a labor contract from 2006 in 2007, resulting in distribution of market and cost of living increases.
- **Other Operating Funds** expenditures are budgeted to increase 15 percent over 2006 primarily due to increased personnel, operating and fuel costs, and the shift of Multi-media Services from the General Fund. Actual expenditures are 10.8 percent behind the same period last year due to several large vehicle purchases made in the first quarter of 2006 (such as a fire engine and dump trucks) and despite the settlement of a labor contract from 2006 in 2007.
- **Water/Sewer Operating Fund** expenditures are budgeted to increase 9.1 percent in 2007 over 2006 due to higher water purchases and sewer treatment costs and increased regional connection charges paid to Cascade Water Alliance (covered by connection charge revenue). Actual expenditures are slightly lower, at 7.1 percent ahead of the same period in 2006, primarily due to position vacancies.
- **Surface Water Management Fund** expenditures are budgeted to increase 14.1 percent in 2007 over 2006 largely due to increased funding for capital projects and additional plans generated from the completed Surface Water Master Plan, and increased personnel costs. Actual expenditures are tracking lower than planned at 9 percent ahead of the same period in 2006 due to position vacancies and despite the settlement of a labor contract from 2006 in 2007.
- **Solid Waste Fund** expenditures are budgeted to increase 7.8 percent in 2007 over 2006 due to higher solid waste contract rates. Actual 2007 expenditures are slightly behind the planned increase at 4.4 percent over the same period in 2006 due to normal variability in disposal contract billing payment amounts.

Expenditures by Fund	Year-to-Date Actual			Budget			% of Budget	
	6/30/2006	6/30/2007	% Change	2006	2007	% Change	2006	2007
<b>General Gov't Operating:</b>								
General Fund	22,465,755	25,125,383	11.8%	49,962,235	54,127,856	8.3%	45.0%	46.4%
Other General Gov't Operating Funds	8,602,686	7,672,374	-10.8%	15,072,831	17,333,688	15.0%	57.1%	44.3%
<b>Total General Gov't Operating</b>	<b>31,068,441</b>	<b>32,797,757</b>	<b>5.6%</b>	<b>65,035,066</b>	<b>71,461,544</b>	<b>9.9%</b>	<b>47.8%</b>	<b>45.9%</b>
<b>Utilities:</b>								
Water/Sewer Operating Fund	8,207,379	8,786,635	7.1%	15,492,943	16,899,618	9.1%	53.0%	52.0%
Surface Water Management Fund	2,314,593	2,522,437	9.0%	4,939,600	5,635,234	14.1%	46.9%	44.8%
Solid Waste Fund	3,671,165	3,832,537	4.4%	7,247,024	7,815,745	7.8%	50.7%	49.0%
<b>Total Utilities</b>	<b>14,193,137</b>	<b>15,141,609</b>	<b>6.7%</b>	<b>27,679,567</b>	<b>30,350,597</b>	<b>9.6%</b>	<b>51.3%</b>	<b>49.9%</b>
<b>Total All Operating Funds</b>	<b>45,261,578</b>	<b>47,939,366</b>	<b>5.9%</b>	<b>92,714,633</b>	<b>101,812,141</b>	<b>9.8%</b>	<b>48.8%</b>	<b>47.1%</b>

\* Budgeted and actual expenditures exclude working capital, operating reserves, capital reserves, and include interfund transfers.

Many revenues are subject to seasonal variability and timing of large receipts can also skew year-to-year comparisons

## General Fund Revenue

- A detailed analysis of **sales tax** revenue can be found starting on page 5.
- Utility tax** revenue is budgeted to increase 10.9 percent ahead of 2006 primarily due to higher utility rates. Actual revenue collection is right on target at 11.1 percent ahead of the same period last year.
- Business licenses and franchise fees** are budgeted to increase 19.8 percent over 2006 primarily due to franchise fees. Actual revenue, at 3 percent ahead of 2006, is running lower than planned so far this year due to a 2% decline in license issuances compared to last year, which is within a normal range of monthly variability between years. The **revenue generating regulatory license** fee is budgeted to increase 8.3 percent over 2006. Actual revenue is up 4.2 percent compared to the same period last year, also due to the number of license issuances.
- Development-related fees** revenue trends are mixed. **Building/structural permits** are budgeted 4.7 higher than 2006, but actual revenue is 28.5 percent lower than

the same period in 2006. **Engineering development charges** are budgeted 56.3 percent higher than 2006 and actual revenues are trailing 2006, down 23.5 percent compared to the same period. **Plan check/development** fees are budgeted 19.8 percent lower than 2006, but actual revenue is 11.7 percent higher compared to 2006. The trends for development-related revenue this year reflect the volatility that is inherent in development activity.

- The year-to-date actual performance comparison between 2006 and 2007 for **other intergovernmental services** is skewed due to a large reimbursement payment received from FEMA in 2006 for firefighters who worked during the Hurricane Katrina relief efforts.
- Fines/forfeits** revenue was expected to remain flat, budgeted 0.4 percent lower than 2006. Actual revenue is up 23.5 percent compared to the same period in 2006 as a result of traffic cases as well as revenue from the new false alarm program.
- Note: Fire District #41 and EMS revenue is normally received in the second half of the year.*

General Fund revenues as of June 30th are over \$1.2 million ahead of the same period in 2006 primarily due to sales and utility taxes.

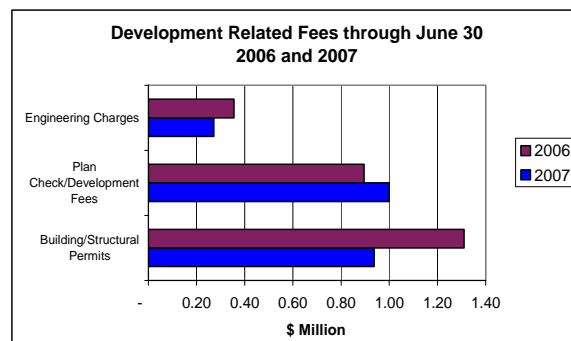
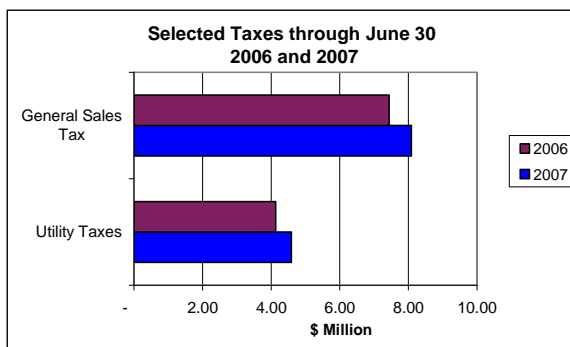
General Fund revenue is budgeted to increase 6.8 percent over 2006. Actual revenue is trailing just slightly, up 5.1 percent over the same period last year due to sales tax anomalies discussed above as well as building-related permits.

The General Fund is the largest of the General Government Operating funds. It is primarily tax supported and accounts for basic services such as public safety, parks and recreation, and community development.

About 355 of the City's 447 employees are budgeted within this fund.

General Fund Resource Category	Year-to-Date Actual			Budget			% of Budget	
	6/30/2006	6/30/2007	% Change	2006	2007	% Change	2006	2007
<b>Taxes:</b>								
Retail Sales Tax: General	7,441,208	8,086,395	8.7%	14,132,692	15,736,923	11.4%	52.7%	51.4%
Retail Sales Tax: Criminal Justice	420,477	550,831	31.0%	890,000	1,025,000	15.2%	47.2%	53.7%
Property Tax	4,267,007	4,531,858	6.2%	8,117,113	8,790,086	8.3%	52.6%	51.6%
Utility Taxes	4,130,223	4,588,082	11.1%	7,171,200	7,950,034	10.9%	57.6%	57.7%
Rev Generating Regulatory License	535,381	512,755	-4.2%	900,000	975,000	8.3%	59.5%	52.6%
Other Taxes	230,169	204,663	-11.1%	464,800	461,000	-0.8%	49.5%	44.4%
<b>Total Taxes</b>	<b>17,024,465</b>	<b>18,474,584</b>	<b>8.5%</b>	<b>31,675,805</b>	<b>34,938,043</b>	<b>10.3%</b>	<b>53.7%</b>	<b>52.9%</b>
<b>Licenses &amp; Permits:</b>								
Building, Structural & Equipment Permits	1,311,108	937,418	-28.5%	2,084,742	2,183,450	4.7%	62.9%	42.9%
Business Licenses/Franchise Fees	711,826	732,932	3.0%	1,184,775	1,418,950	19.8%	60.1%	51.7%
Other Licenses & Permits	131,765	88,240	-33.0%	169,020	169,900	0.5%	78.0%	51.9%
<b>Total Licenses &amp; Permits</b>	<b>2,154,699</b>	<b>1,758,590</b>	<b>-18.4%</b>	<b>3,438,537</b>	<b>3,772,300</b>	<b>9.7%</b>	<b>62.7%</b>	<b>46.6%</b>
<b>Intergovernmental:</b>								
Grants	66,671	98,795	48.2%	207,017	169,454	-18.1%	32.2%	58.3%
State Shared Revenues & Entitlements	268,746	331,428	23.3%	590,033	606,715	2.8%	45.5%	54.6%
Fire District #41	-	-	N/A	3,141,052	3,329,121	N/A	N/A	N/A
EMS	-	-	N/A	489,685	504,376	N/A	N/A	N/A
Other Intergovernmental Services	393,069	296,068	-24.7%	438,539	423,870	-3.3%	89.6%	69.8%
<b>Total Intergovernmental</b>	<b>728,486</b>	<b>726,291</b>	<b>-0.3%</b>	<b>4,866,326</b>	<b>5,033,536</b>	<b>3.4%</b>	<b>15.0%</b>	<b>14.4%</b>
<b>Charges for Services:</b>								
Internal Charges	1,676,590	1,710,072	2.0%	3,531,586	3,365,127	-4.7%	47.5%	50.8%
Engineering Services	355,352	271,776	-23.5%	400,000	625,000	56.3%	88.8%	43.5%
Plan Check & Development Fees	895,650	1,000,215	11.7%	2,276,836	1,825,900	-19.8%	39.3%	54.8%
Recreation	40,136	38,824	-3.3%	74,000	81,000	9.5%	54.2%	47.9%
Other Charges for Services	320,761	459,898	43.4%	674,199	752,591	11.6%	47.6%	61.1%
<b>Total Charges for Services</b>	<b>3,288,489</b>	<b>3,480,785</b>	<b>5.8%</b>	<b>6,956,621</b>	<b>6,649,618</b>	<b>-4.4%</b>	<b>47.3%</b>	<b>52.3%</b>
<b>Fines &amp; Forfeits</b>	<b>451,089</b>	<b>557,145</b>	<b>23.5%</b>	<b>1,157,550</b>	<b>1,152,750</b>	<b>-0.4%</b>	<b>39.0%</b>	<b>48.3%</b>
<b>Miscellaneous</b>	<b>327,148</b>	<b>191,806</b>	<b>-41.4%</b>	<b>590,991</b>	<b>408,065</b>	<b>-31.0%</b>	<b>55.4%</b>	<b>47.0%</b>
<b>Total Revenues</b>	<b>23,974,376</b>	<b>25,189,201</b>	<b>5.1%</b>	<b>48,685,830</b>	<b>51,954,312</b>	<b>6.7%</b>	<b>49.2%</b>	<b>48.5%</b>
<b>Other Financing Sources:</b>								
Interfund Transfers	-	-	N/A	405,986	491,398	N/A	N/A	N/A
<b>Total Other Financing Sources</b>	<b>-</b>	<b>-</b>	<b>N/A</b>	<b>405,986</b>	<b>491,398</b>	<b>N/A</b>	<b>N/A</b>	<b>N/A</b>
<b>Total Resources</b>	<b>23,974,376</b>	<b>25,189,201</b>	<b>5.1%</b>	<b>49,091,816</b>	<b>52,445,710</b>	<b>6.8%</b>	<b>48.8%</b>	<b>48.0%</b>

\* Budgeted and actual revenues exclude resources forward.

General Fund Revenue *continued*

## General Fund Expenditures

General Fund Department Expenditures	Year-to-Date Actual			Budget			% of Budget	
	6/30/2006	6/30/2007	% Change	2006	2007	% Change	2006	2007
Non-Departmental	389,777	472,296	21.2%	851,614	1,128,527	32.5%	45.8%	41.9%
City Council	200,408	182,545	-8.9%	311,733	316,392	1.5%	64.3%	57.7%
City Manager's Office	1,219,349	1,421,741	16.6%	2,431,813	3,343,442	37.5%	50.1%	42.5%
Human Resources	446,309	490,228	9.8%	855,969	1,036,649	21.1%	52.1%	47.3%
City Attorney's Office	409,516	433,438	5.8%	881,406	997,460	13.2%	46.5%	43.5%
Parks & Community Services	2,165,850	2,471,573	14.1%	5,096,976	5,867,551	15.1%	42.5%	42.1%
Public Works (Engineering)	1,412,934	1,759,699	24.5%	2,887,897	3,792,206	31.3%	48.9%	46.4%
Finance and Administration	1,409,977	1,670,064	18.4%	2,891,824	3,508,508	21.3%	48.8%	47.6%
Planning & Community Development	1,413,715	1,588,264	12.3%	2,965,328	3,824,113	29.0%	47.7%	41.5%
Police	6,005,517	6,442,467	7.3%	12,962,506	13,812,086	6.6%	46.3%	46.6%
Fire & Building	7,143,160	7,942,915	11.2%	14,578,689	15,795,562	8.3%	49.0%	50.3%
<b>Total Expenditures</b>	<b>22,216,512</b>	<b>24,875,230</b>	<b>12.0%</b>	<b>46,715,755</b>	<b>53,422,496</b>	<b>14.4%</b>	<b>47.6%</b>	<b>46.6%</b>
<b>Other Financing Uses:</b>								
Interfund Transfers	249,243	250,153	0.4%	3,246,480	705,360	-78.3%	7.7%	35.5%
<b>Total Other Financing Uses</b>	<b>249,243</b>	<b>250,153</b>	<b>0.4%</b>	<b>3,246,480</b>	<b>705,360</b>	<b>-78.3%</b>	<b>7.7%</b>	<b>35.5%</b>
<b>Total Expenditures &amp; Other Uses</b>	<b>22,465,755</b>	<b>25,125,383</b>	<b>12.3%</b>	<b>49,962,235</b>	<b>54,127,856</b>	<b>8.3%</b>	<b>45.0%</b>	<b>46.4%</b>

\* Budgeted and actual expenditures exclude working capital, operating reserves, and capital reserves.

- The **Non-departmental** division expenditures are budgeted 32.5 percent higher than 2006 due to a relocation of the Multi-media Services functions to Information Technology resulting in a change in accounting for the internal charges. Actual expenditures are 21.2 percent higher than the same period in 2006 primarily due to the timing of outside agency payments.

Budgeted and current year actual expenditures compared to 2006 for the following departments are up primarily due to higher personnel costs, including an unsettled labor contract from 2006 that settled in 2007 and additional positions added in 2007. In addition to this general trend, specific highlights by selected department are listed below:

- The **City Manager's** expenditures are budgeted 37.5 percent higher than 2006 due the addition of a communications program manager and municipal court staffing, additional funding for economic development, outside agencies and one-time annexation studies. Actual expenditures are only 16.6 percent ahead of the same period last year primarily due to the normal delay in hiring newly approved positions and uncompleted projects.
- The **Human Resources Department** expenditures are budgeted 21.1 percent higher than 2006 due to an additional temporary human resources analyst. Actual expenditures are only 9.8 percent ahead of the same period last year due to the delay of hiring the new position.

**Compared to budget, 2007 General Fund actual expenditures are tracking slightly below the same trend as last year (46.6 percent of budget in 2007 compared to 47.6 percent of budget in 2006) largely due to the normal delayed hiring of newly approved 2007 positions, position vacancies, and timing of major projects.**

(Continued on page 5)

### General Fund expenditures *continued*



Downtown Kirkland fountain at Park Lane

- The **Public Works Department** expenditures are budgeted 31.3 percent higher than 2006 due to additional positions, service packages for traffic counts and transportation management plans, as well as one-time annexation studies. Actual expenditures are lower than planned, 24.5 percent higher than the same period in 2006, due to position vacancies, the delay of hiring new positions, and unfinished projects.
- The **Finance & Administration Department** expenditures are budgeted 21.3 percent higher than 2006 due to additional utility billing staff and one-time annexation studies. Actual expenditures are trailing slightly, at 18.4 higher than the same period in 2006, due to uncompleted projects, such as annexation.
- The **Planning Department** expenditures are budgeted 29 percent higher than 2006 due to additional development-related staffing and one-time annexation studies. Actual expenditures are lower than planned, only 12.3 percent ahead compared to the same period last year, due to the delay in hiring additional staffing and uncompleted projects such as the Shoreline Master and Downtown Strategic Plans.
- The **Fire & Building Department** expenditures are budgeted 8.3 percent higher than 2006 due to additional development staff and a temporary emergency preparedness coordinator. Actual expenditures are higher than planned, 11.2 percent ahead compared to the same period last year primarily due to 2006 staff vacancies and one-time expenditures for computer-aided dispatch software and Emergency Operation Center laptop computers in 2007.

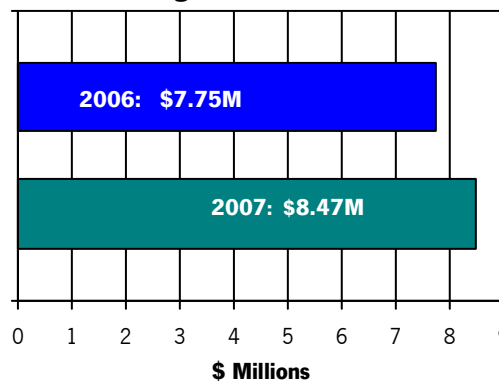
## Sales Tax Revenue Analysis

2007 sales tax revenue is **up 9.4 percent** compared to the same period in 2006 primarily due to strong performance in the auto/gas retail, contracting sectors, and miscellaneous sectors (see table on page 6).

### Review by business sectors:

- The **miscellaneous** sector is **up 68 percent** due to a significant one-time receipt.
- **Auto/gas retail** is the largest “ongoing” contributor to the sales tax revenue increase so far this year, **up 18 percent** compared to the same period last year due to strong performance of several key retailers, as well as two new smaller retailers.
- **General merchandise/miscellaneous retail** is **up 3.2 percent** over the same period last year due to moderately strong performance by key retailers.
- **Retail eating/drinking** is **up 6.1 percent** compared to the same period last year primarily due to the collection of a past-due account from prior years; factoring this out this sector is up only 1.9 percent.
- **Other retail declined 2.7 percent** over the same period last year due to closure of two major retailers and one-time anomalies in the retail food and health care sectors in 2006 that skew comparisons between the years.
- Business sectors impacted by development-related activity (contracting, wholesale, services and communications) are posting mixed results in 2007 compared to the same period last year. Comparing to the same period last year: **contracting** is **up 12.1 percent**, which is impressive since 2006 was a record year; the **services** sector is **up 5.4 percent** reflecting generally strong performance from development as well as a new hotel; the **communications** sector is **up 32.6 percent** due to strong development-related activity; and **wholesale** is **down 24 percent**, reflective more of the unusually strong performance in 2006 rather than a weakness in 2007.

Sales Tax Receipts  
through June 2006 & 2007



Auto/gas retail is the star performer so far this year.

Development-related sales tax revenue remains strong in 2007.

As of the first quarter 2007, Kirkland is the 19th largest city in the state in population, but ranks 13th in sales tax revenue.

In King County, Kirkland is the 9th largest city, but ranks 7th in sales tax revenue as of the first quarter of 2007.

**City of Kirkland Total Actual Sales Tax Receipts**

Business Sector Group	Jan - June		Dollar Change	Percent Change	Percent of Total	
	2006	2007			2006	2007
Services	786,897	829,278	42,381	5.4%	10.2%	9.8%
Contracting	1,501,882	1,683,438	181,556	12.1%	19.4%	19.9%
Communications	272,672	361,578	88,906	32.6%	3.5%	4.3%
Auto/Gas Retail	1,356,289	1,600,876	244,587	18.0%	17.5%	18.9%
Gen Merch/Misc Retail	1,207,758	1,246,787	39,029	3.2%	15.6%	14.7%
Retail Eating/Drinking	580,290	615,879	35,589	6.1%	7.5%	7.3%
Other Retail	889,709	865,574	-24,135	-2.7%	11.5%	10.2%
Wholesale	722,992	549,782	-173,210	-24.0%	9.3%	6.5%
Miscellaneous	427,420	718,196	290,776	68.0%	5.5%	8.4%
<b>Total</b>	<b>7,745,909</b>	<b>8,471,388</b>	<b>725,479</b>	<b>9.4%</b>	<b>100.0%</b>	<b>100.0%</b>

*Kirkland's sales tax base is comprised of a variety of businesses which are grouped and analyzed by business sector (according to NAICS, or "North American Industry Classification System"). Nine business sector groupings are used to compare 2006 and 2007 year-to-date sales tax receipts in the table to the left.*

**City of Kirkland Sales Tax Receipts by Month**

Month	Sales Tax Receipts		Dollar Change	Percent Change
	2006	2007		
January	1,116,572	1,267,021	150,449	13.5%
February	1,821,021	1,525,665	(295,356)	-16.2%
March	1,126,328	1,154,890	28,562	2.5%
April	1,061,134	1,604,395	543,261	51.2%
May	1,309,595	1,496,755	187,160	14.3%
June	1,311,259	1,422,662	111,403	8.5%
<b>Total</b>	<b>7,745,909</b>	<b>8,471,388</b>	<b>725,479</b>	<b>9.4%</b>

*When analyzing monthly sales tax receipts, there are two items of special note: First, most businesses remit their sales tax collections to the Washington State Department of Revenue on a monthly basis. Small businesses only have to remit their sales tax collections either quarterly or annually, which can create anomalies when comparing the same month between two years. Second, for those businesses which remit sales tax monthly, there is a two month lag from the time that sales tax is collected to the time it is distributed to the City. For example, sales tax received by the City in June 2007 is for sales actually made in April 2007. Monthly sales tax receipts through June 2006 and 2007 are compared in the table to the left.*

**One-time spikes (in development-related revenue in February 2006 and the miscellaneous category and development-related revenue in April 2007) skew monthly comparisons between the years.**

*Kirkland's sales tax base is further broken down by business district (according to geographic area), as well as "unassigned or no district" for small businesses and businesses with no physical presence in Kirkland.*

**Totem Lake**, which accounts for almost 30 percent of the total sales tax receipts, is **up 10.8 percent** over the same period last year primarily due to strong performance in auto/gas retail and a new hotel, and despite the closure of a major super-market and electronics store.

Almost 60 percent of this business district's revenue comes from the

auto/gas retail and general merchandise/retail apparel sectors.

**NE 85<sup>th</sup> Street**, which accounts for almost 14 percent of the total sales tax receipts, is **up 9 percent** over the same period last year primarily due to the retail automotive/gas and general merchandise/miscellaneous retail sectors. Over 80 percent of this business district's revenue comes from these two business sectors.

**Downtown**, which accounts for over 6 percent of the total sales tax receipts, is **up 5.9 percent** over the same period last year primarily due to collections on a past due account in the retail eating/drinking

sector and strong performance in the retail food sector. The retail eating/drinking sector provides almost 40 percent of this business district's revenue.

**Houghton & Bridle Trails**, which accounts for over 3 percent of the total sales tax receipts, is **up 24.8 percent** almost entirely due to miscellaneous retail, which also provides almost 40 percent of these business districts' revenue.

**Carillon Point & Yarrow Bay**, which accounts for almost 3 percent of the total sales tax receipts, is **down 2.3 percent** reflecting the inherent volatility of software/technology companies' performance and despite strong performance in the business services sector. Almost 80 percent of this business district's revenue comes from business services, retail eating/drinking and hotels.

**Juanita**, which accounts for almost 2 percent of the total sales tax receipts, is **up 14.3 percent** largely due to the "retail eating/drinking" sector, which also provides 46 percent of this business district's revenue.

When reviewing sales tax receipts by business district, it's important to point out that over 44 percent of the revenue received in 2007 is in the "unassigned or no district" category largely due to strong contracting revenue, but it also reflects increasing revenue from Internet and catalog sales from businesses located outside of the City. Revenue in this category is up 8.6 percent over the same period last year.

#### City of Kirkland Sales Tax by Business District

Business District	Jan - Jun Receipts		Dollar Change	Percent Change	Percent of Total	
	2006	2007			2006	2007
Totem Lake	2,259,716	2,503,612	243,896	10.8%	29.2%	29.6%
NE 85th St	1,068,425	1,164,981	96,556	9.0%	13.8%	13.8%
Downtown	515,605	545,825	30,220	5.9%	6.7%	6.4%
Carillon Pt & Yarrow Bay	228,197	222,952	-5,245	-2.3%	2.9%	2.6%
Houghton & Bridle Trails	229,219	286,069	56,850	24.8%	3.0%	3.4%
Juanita	130,195	148,834	18,639	14.3%	1.7%	1.8%
Unassigned or No District:						
Contracting	1,501,882	1,683,438	181,556	12.1%	19.4%	19.9%
Other	1,812,670	1,915,677	103,007	5.7%	25.0%	24.3%
<b>Total</b>	<b>7,745,909</b>	<b>8,471,388</b>	<b>725,479</b>	<b>9.4%</b>	<b>100.0%</b>	<b>100.0%</b>

#### Sales Tax Revenue Outlook

Sales tax revenue remains strong in 2007, up 9.4 percent over the same period in 2006 (which was a record year). However, a large percentage of this revenue is from highly volatile one-time development-related activity, which cannot be relied upon to fund ongoing services. The monthly volatility is illustrated in February 2006 and April 2007. If these sectors were performing at a more typical growth rate (6 percent), total revenue would be up 6.8 percent over last year instead of 9.4 percent.

Opportunities for growth exist from the redevelopment of Totem Lake Mall and Park Place, current major expansions at key automobile dealerships, and the hotel that opened last year and one currently under construction downtown. A major new risk on the horizon is the recent proposal from Costco to locate new stores in Bellevue and Redmond. Additionally, the economic recession a few years ago and the current reliance on construction-related sales tax growth serve as reminders that sales tax is an economically sensitive revenue source. In good times, sales tax growth easily outpaces the rate of inflation and is an attractive funding source for service packages. However, when a downturn occurs, the City's financial ability to maintain existing services can be quickly threatened. Additional volatility is created by gaining or losing significant businesses, shifts in construction activity due to economic conditions, and one-time field audit recoveries.

#### OFFICE VACANCIES:

Eastside vacancy rates remain low at 9.45 percent at the end of the second quarter 2007 compared to 24 percent in 2003 according to CB Richard Ellis Real Estate Services. Kirkland's vacancy rate is 5.47 percent as of the second quarter of 2007.

#### LODGING TAX REVENUE:

Lodging tax revenue is up 60 percent compared to the same period last year due to overall strong performance in the accommodations industry as well as the new hotel in Totem Lake.

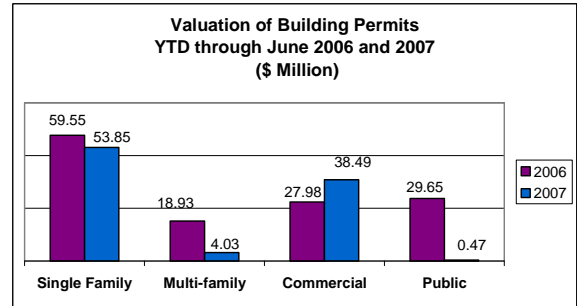
#### Economic Environment Update

Local job growth remains strong in 2007, especially in the important aerospace and technology sectors. The Seattle-Tacoma metropolitan area added over 105,000 jobs since January 2005 and the unemployment rate in King County dropped to 4 percent as of June 2007, below the national average of 4.7 percent. Conway & Pedersen's *Economic Forecaster* predicts more than 100,000 jobs will be added to the Puget Sound market over the next two years. According to the Hebert Research-Business Journal Business Confidence Index, local executives are more confident now than the previous two quarters about the local economy. The positive report continues a 3-year run of better-than-average index scores, which is atypical according to Jim Hebert of Hebert Research. One of the concerns by local executives is the skilled labor shortage along with rising energy costs. Another local economic index that uses information from a survey by local purchasing managers (Western Washington Chapter of the National Purchasing Managers) decreased slightly in June, down 0.9 points from the previous month to 68.1. (It should be noted that a score of more than 50 points signals an expanding economy, while a score of less than 50 points indicates a shrinking economy.)

Other positive local regional economic indicators:

- ◆ Taxable retail sales in King County are up 9.3 percent for the first quarter 2007 compared to first quarter of 2006.
- ◆ As of the second quarter of 2007, the Puget Sound office market saw its 16th quarter of positive absorption, with almost 1.2 million square feet of previously vacant space filled. There is almost 4.8 million square feet currently under construction to meet the demands of the expansion of local companies for office space.
- ◆ First quarter 2007 exports of goods originating in Washington State increased 10.6 percent over first quarter 2006, primarily from transportation equipment.

Local **development-activity** through June 2006 and 2007 as measured by the valuation of City of Kirkland building permits is illustrated in the chart to the right. Activity remains relatively strong, especially in the commercial sector. While single family activity in 2007 falls below 2006 levels, it still remains very strong compared to normal historical trends. The significant spike in 2006 public activity reflects the permitting for Evergreen Hospital. Plan check fees (a leading indicator of development activity) are up in 2007 compared to the same period in 2006, so an upswing in building permit activity may follow.



In regard to **housing prices and sales**, while pending sales of new and existing homes in King County are down 9.4 percent in June 2007 compared with a year earlier, prices rose 7.1 percent. Realtors are forecasting that home prices in the Puget Sound region could drop by 1.4 percent by the end of the year; this would be the first annual price decline in more than 40 years. However, not all neighborhoods are expected to react the same depending on inventory and demand. The Eastside is considered to be a balanced market because of strong job growth creating demand, so prices may remain stable. Nationally, home sales fell in June for a fourth consecutive month and the median price edged up slightly. However, on a national basis, analysts are expecting prices to fall due to the high level of unsold homes.

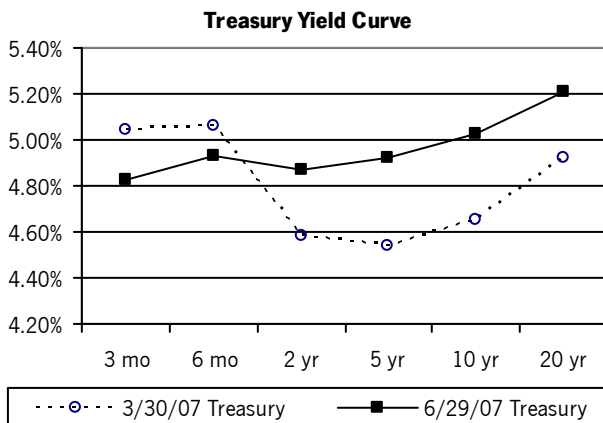
**Seattle metro CPI** continues to track higher than the national average (3.31 percent compared to the national average of 2.7 percent as of June). (However, this is a dip from the Seattle index for April, which was 3.9 percent.) The June 2007 CPI is used to calculate City employee cost of living adjustments for 2008. As a result, 2008 COLA's will range from 2.98 to 3.31 percent depending on the bargaining unit contract.

## Investment Report

### MARKET OVERVIEW

The Fed Funds rate remained at 5.25 percent through the second quarter of 2007.

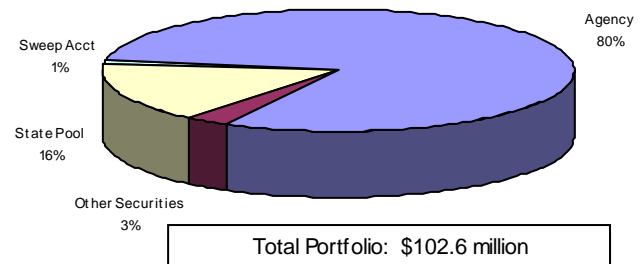
The yield curve rose in the one to twenty year range while short term rates decreased. The result is a more normal yield curve with long term rates above the short term rates. Economic indicators continue to be mixed.



### Diversification

The City's current investment portfolio is composed of Government Agency bonds, State and Local Government bonds, US Treasury notes, the State Investment Pool and an overnight bank sweep account. City investment procedures allow for 100% of the portfolio to be invested in US Treasury or Federal Government obligations.

### Investments by Category



### CITY PORTFOLIO

It is the policy of the City of Kirkland to invest public funds in a manner which provides the highest investment return with maximum security while meeting the City's daily cash flow requirements and conforming to all Washington state statutes governing the investment of public funds.

The primary objectives for the City of Kirkland's investment activities are: legality, safety, liquidity and yield. Additionally, the City diversifies its investments according to established maximum allowable exposure limits so that reliance on any one issuer will not place an undue financial burden on the City. The City's portfolio increased in the 2<sup>nd</sup> quarter of 2007 primarily due to property tax collections in April and May. On June 30, 2007 the total portfolio was \$102.6 million compared to \$95.3 million on March 31, 2007.

## 2007 ECONOMIC OUT-LOOK and INVESTMENT STRATEGY

The forecast for the U.S. economy growth has been slightly reduced during the second quarter. GDP growth for 2007 is now expected to be 2.1 percent and CPI inflation at 2.3 percent. Beyond the very short term, the forecasters see little threat of accelerating inflation. The unemployment rate is expected to average 4.6 percent this year, down from earlier estimates of 4.7 percent.

June reports indicated that Fed Funds rate were expected to remain at 5.25 percent through the end of 2007. Recent market volatility may cause the Fed Fund rate to fall before the end of the year.

Investments will be purchased as opportunities are available to obtain a return above the State Pool which is currently near 5.2 percent. We will continue to watch the economy closely and maintain portfolio duration within target range as interest rates level off. Total budgeted investment income for 2007 is \$4 million.

## Investment Report *continued*

### Liquidity

The target duration for the City's portfolio is based on the 2 year treasury rate which increased from 4.58 percent on March 31, 2007 to 4.87 percent on June 29, 2007. The average maturity of the City's investment portfolio increased from 1.32 years on March 31, 2007 to 1.62 years on June 30, 2007. The duration is slightly above the target as longer term securities were purchased in mid June when the 2 year Treasury Note rate was above 5%.

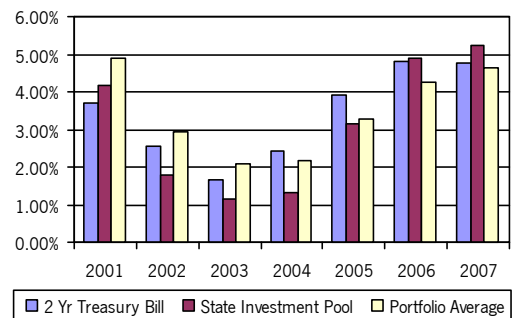
### Yield

The City Portfolio yield to maturity increased from 4.56 percent on March 31, 2007 to 4.79 percent on June 30, 2007. Through June 30, 2007, the City's annual average yield to maturity was 4.65 percent, which performed under the State Investment Pool annual average yield to maturity at 5.23 percent and was below the 2 Year Treasury note annual average for 2007 at 4.76 percent.

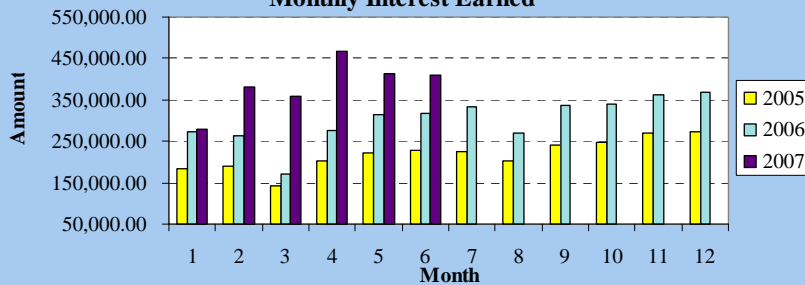
The City's practice of investing further out on the yield curve than the State Investment Pool results in earnings higher than the State Pool during declining interest rates and lower earnings than the State Pool during periods of rising interest rates. This can be seen in the adjacent graph.

Benchmark Comparison	March 31, 2007	June 30, 2007
City Yield to Maturity (YTM)	4.56%	4.79%
City Annual Average YTM	4.56%	4.65%
City Year to Date Cash Yield	3.12%	4.40%
State Pool Average Yield	5.24%	5.23%
2 yr Treasury Note Avg YTM	4.72%	4.76%

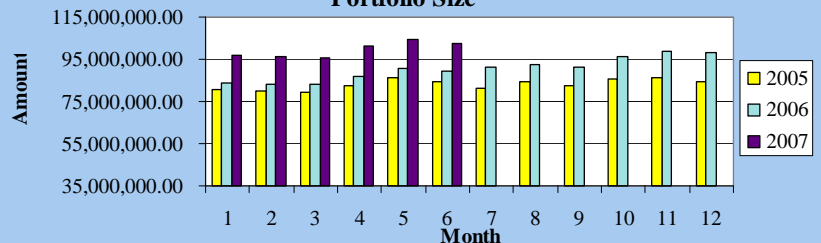
Investment Interest Rate Comparisons



Monthly Interest Earned



Portfolio Size



## Reserve Summary

### General Operating Reserve

For the City's "Rainy Day" fund, the target is established by fiscal policy at five percent of the operating budget (excluding utility and internal service funds). Each year, the target amount will change proportional to the change in the operating budget. To maintain full funding, the increment between five percent of the previous year's budget and the current budget would be added or subtracted utilizing interest income and year-end transfers from the General Fund. It is a reserve to be used for unforeseen revenue losses and other temporary events. If the reserve is utilized by the City Council, the authorization should be accompanied by a plan for replenishing the reserve within a two to three year period.

### Revenue Stabilization Reserve

The Revenue Stabilization Reserve was approved by Council in July 2003 and was created by segregating a portion of the General Operating Reserve. The purpose of this reserve is to provide an easy mechanism to tap reserves to address temporary revenue shortfalls resulting from temporary circumstances (e.g. economic cycles, weather-related fluctuations in revenue). Council set the target at ten percent of selected General Fund revenue sources which are subject to volatility (e.g. sales tax, development fees and utility taxes). The Revenue Stabilization Reserve may be used in its entirety; however, replenishing the reserve will constitute the first priority for use of year-end transfers from the General Fund.

### Contingency Fund

The Contingency Fund was established pursuant to RCW 35A.33.145 to "provide monies with which to meet any municipal expense, the necessity or extent of which could not have been foreseen or reasonably evaluated at the time of adopting the annual budget." State law sets the maximum balance in the fund at \$.375 per \$1,000 of assessed valuation. This reserve would be used to address unforeseen expenditures (as opposed to revenue shortfalls addressed by the Revenue Stabilization Reserve). The fund can be replenished through interest earnings up to the maximum balance or through the year-end transfer if needed. project).

*Reserves are an important indicator of the City's fiscal health. They effectively represent "savings accounts" that are established to meet unforeseen budgetary needs (general purpose reserves) or are otherwise dedicated to a specific purpose (special purpose reserves). The City's reserves are listed with their revised estimated balances at the end of the biennium in the table below:*

Reserves	2007-08 Est End Balance	2007 Auth. Uses	2007 Auth. Additions	Revised 2007-08 End Balance
<b>GENERAL PURPOSE RESERVES</b>				
Contingency	3,193,826	85,936		3,107,890
General Capital Contingency	3,312,834			3,312,834
Park & Municipal Reserve:				
General Oper. Reserve (Rainy Day)	2,712,836			2,712,836
Revenue Stabilization Reserve	2,082,380			2,082,380
Building & Property Reserve	1,316,124	10,000		1,306,124
Council Special Projects Reserve	309,960	15,000		294,960
<b>Total General Purpose Reserves</b>	<b>12,927,960</b>	<b>110,936</b>	<b>0</b>	<b>12,817,024</b>
<b>SPECIAL PURPOSE RESERVES</b>				
Excise Tax Capital Improvement:				
REET 1	6,673,678	791,394		5,882,284
REET 2	6,067,898			6,067,898
Equipment Rental:				
Vehicle Reserve	5,907,138			5,907,138
Radio Reserve	36,000			36,000
Information Technology:				
PC Replacement Reserve	453,670			453,670
Major Systems Replacement Reserve	666,500			666,500
Facilities Maintenance:				
Operating Reserve	550,000			550,000
Facilities Sinking Fund	1,439,951			1,439,951
Impact Fees				
Roads	1,984,145			1,984,145
Parks	920,086			920,086
Park Bond Reserve	502,916			502,916
Cemetery Improvement	476,401			476,401
Off-Street Parking	29,564			29,564
Tour Dock	73,211			73,211
Street Improvement	1,121,498	161,100		960,398
Firefighter's Pension	1,359,860			1,359,860
Park & Municipal Reserve:				
Litigation Reserve	20,004			20,004
Labor Relations Reserve	51,255			51,255
Police Equipment Reserve	26,519			26,519
LEOFF 1 Police Reserve	625,754			625,754
Facilities Expansion Reserve	800,000			800,000
Development Services Reserve	1,290,831			1,290,831
Tree Ordinance	13,750			13,750
Donation Accounts	143,859			143,859
Revolving Accounts	148,606			148,606
Water/Sewer Operating Reserve	1,511,245			1,511,245
Water/Sewer Debt Service Reserve	820,155			820,155
Water/Sewer Capital Contingency	1,703,640	113,900		1,589,740
Water/Sewer Construction Reserve	8,738,358	350,000		8,388,358
Surface Water Operating Reserve	320,299			320,299
Surface Water Capital Contingency	876,760	202,000		674,760
Surface Water-Transp. Related Rsv	1,417,365			1,417,365
Surface Water Construction Reserve	1,240,563			1,240,563
<b>Total Special Purpose Reserves</b>	<b>48,011,479</b>	<b>1,618,394</b>	<b>0</b>	<b>46,393,085</b>
<b>Grand Total</b>	<b>60,939,439</b>	<b>1,729,330</b>	<b>0</b>	<b>59,210,109</b>

### Reserve Summary *continued*

RESERVE	AMOUNT	DESCRIPTION
<b>2007 Council Authorized Uses</b>	<b>\$1,729,330</b>	
Contingency Fund	\$31,500	Funding for phase 1 of the Permit Process Improvement Project to review the single family building permit process.
	\$54,436	Funding for continued public outreach for Phase II of the annexation study.
Building/Property Reserve	\$10,000	Funding for a study of the Peter Kirk restroom to coincide with the timing of the design for the downtown transit center.
Council Special Projects Reserve	\$15,000	Funding for the Assistance League of the Eastside's Operation School Bell program.
Real Estate Excise Tax (REET) 1 Reserve	\$235,840	Funding for the purchase of the Irvin Property in the Yarrow Bay Wetlands.
	\$362,354	Funding for purchase of greenbelt property near Everest Park.
	\$193,200	Funding for purchase of Niedermeier property near Everest Park.
Street Improvement Reserve	\$91,100	Additional funding for completion of the Central Way Improvements project (street portion).
	\$70,000	Additional funding for the 2007 Pavement Striping Program.
Water/Sewer Capital Contingency	\$113,900	Additional funding for completion of the Central Way Improvements project (utilities portion).
Water/Sewer Construction Reserve	\$350,000	Additional funding to complete the 2007 Emergency Sewer Program.
Surface Water Capital Contingency	\$202,000	Additional funding for the Juanita Creek Channel Enhancement project.

**2007 Council Authorized Additions** **\$0**

No Council Authorized Additions as of June 30, 2007.

*The summary schedule in the table above details all Council authorized uses and additions to each reserve through June 2007.*

Reserves	Revised 2007-08 End Balance	2007-08 Target	Over (Under) Target
<b>GENERAL PURPOSE RESERVES</b>			
Contingency	3,107,890	3,698,455	(590,565)
General Capital Contingency	3,312,834	5,822,280	(2,509,446)
Park & Municipal Reserve:			
General Oper. Reserve (Rainy Day)	2,712,836	3,134,779	(421,943)
Revenue Stabilization Reserve	2,082,380	2,143,422	(61,042)
Council Special Projects Reserve	294,960	250,000	44,960
<b>General Purpose Reserves with Targets</b>	<b>11,510,900</b>	<b>15,048,936</b>	<b>(3,538,036)</b>
<b>SPECIAL PURPOSE RESERVES</b>			
Excise Tax Capital Improvement:			
REET 1	5,882,284	1,435,000	4,447,284
REET 2	6,067,898	4,959,200	1,108,698
Information Technology:			
Major Systems Replacement Reserve	666,500	1,025,000	(358,500)
Firefighter's Pension	1,359,860	1,103,000	256,860
Park & Municipal Reserve:			
Litigation Reserve	20,004	50,000	(29,996)
LEOFF 1 Police Reserve	625,754	855,000	(229,246)
Development Services Reserve	1,290,831	1,290,831	0
Water/Sewer Operating Reserve	1,511,245	1,511,245	0
Water/Sewer Debt Service Reserve	820,155	820,155	0
Water/Sewer Capital Contingency	1,589,740	1,703,640	(113,900)
Surface Water Operating Reserve	320,299	320,299	0
Surface Water Capital Contingency	674,760	876,760	(202,000)
<b>Special Purpose Reserves with Targets</b>	<b>20,829,330</b>	<b>15,950,130</b>	<b>4,879,200</b>
<b>Reserves without Targets</b>	<b>26,869,879</b>	<b>n/a</b>	<b>n/a</b>
<b>Total Reserves</b>	<b>59,210,109</b>	<b>n/a</b>	<b>n/a</b>

*The table to the left compares the revised ending balance to the targets established in the budget process.*



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[www.ci.kirkland.wa.us](http://www.ci.kirkland.wa.us)

The **Financial Management Report (FMR)** is a high-level status report on the City's financial condition that is produced quarterly.

- It provides a summary **budget to actual** comparison for year-to-date revenues and expenditures for all operating funds. The report also compares this year's actual revenue and expenditure performance to the prior year.
- The **Sales Tax Revenue Analysis Report** takes a closer look at the City's largest and most economically sensitive revenue source.
- **Economic environment** information provides a brief outlook at the key economic indicators for the Eastside and Kirkland such as office vacancies, residential housing prices/sales, development activity, inflation and unemployment.
- The **Investment Summary** report includes a brief market overview, a snapshot of the City's investment portfolio, and the City's year-to-date investment performance.
- The **Reserve Summary** report highlights the uses of and additions to the City's reserves in the current year as well as the projected ending reserve balance relative to each reserve's target amount.

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- Washington State Department of Revenue
- U.S. Bureau of Labor Statistics
- City of Kirkland Building Division
- City of Kirkland Finance Department